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In The

Supreme Court of the United States

CORRECTED COPY

GULF INSURANCE COMPANY,

Petitioner,

v.

SIEGFRIED CONSTRUCTION, INCORPORATED,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Petition for Writ of Certiorari

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44 pp

QUESTION PRESENTED

Does a performance bond's condition precedent that the principal be in default and that the obligee declare the principal to be in default require termination of the principal to invoke a surety's obligations under that performance bond?

PARTIES TO THE PROCEEDING

The parties to the proceeding in the Fourth Circuit Court of Appeals were Gulf Insurance Company and Siegfried Construction, Inc. Associated Builders and Contractors of Virginia, Inc., The Surety Association of America and American Insurance Association participated as *Amici Curiae* before the Fourth Circuit Court of Appeals.

CORPORATE DISCLOSURE

Petitioner, Gulf Insurance Company, is not a publicly held entity. Citigroup, Inc. and Travelers Property Casualty Corporation are both publicly held entities that own ten percent (10%) or more of Gulf Insurance Company's stock.

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Petitioner, Gulf Insurance Company, respectfully requests that a writ of certiorari be issued to review the judgment of the United States Court of Appeals for the Fourth Circuit in this case.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Fourth Circuit is not published, but can be found at *Siegfried Construction, Inc. v. Gulf Insurance Company*, 2000 WL 123944 (2000) and is reproduced as Appendix A. The opinion of the United States District Court for the Eastern District of Virginia, Civil Action No. 98-555-A (E.D.Va. 1998) was rendered as an oral opinion and is reproduced from the transcript as Appendix B.

STATEMENT OF JURISDICTION

The judgment of the United States Court of Appeals for the Fourth Circuit was entered on February 2, 2000. No petition for rehearing was filed.

The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

No constitutional or statutory provisions are involved in this case.

STATEMENT OF THE CASE

The fundamental question in this case is whether an obligee on a performance bond is required to terminate the principal to invoke the surety's obligation under the bond.

A. The Underlying Events

Jennifer Builders, Inc. (hereinafter "Jennifer Builders" or "Principal") entered into a subcontract with Siegfried Construction, Inc. (hereinafter "Siegfried" or "Obligee") to perform construction and renovation work on a three-story hotel known as the Sleep Inn Hotel (hereinafter the "Project"). Jennifer Builders' subcontract with Siegfried required that Jennifer Builders obtain a performance bond. Gulf Insurance Company (hereinafter known as "Gulf" or the "Surety") issued a performance bond on behalf of Jennifer Builders. Siegfried accepted the performance bond provided by Gulf. The explicit terms of the performance bond read as follows:

> NOW, THEREFORE, THE CONDITION OF THIS OBLIGATION is such that, if Principal shall promptly and faithfully perform said subcontract, then this obligation shall be null and void; otherwise to remain in full force and effect.
>
> WHENEVER Principal shall be, and be declared by Obligee to be in default under the subcontract, the Obligee having performed Obligee's obligations thereunder:
>
> 1. Surety may promptly remedy the default subject to the provisions of paragraph 3 herein, or;
> 2. Obligee, after reasonable notice to Surety may, or Surety upon demand of Obligee may, arrange for the performance of Principal's obligation under the subcontract subject to the provisions of paragraph 3 herein;

> 3. The balance of the subcontract price, as defined below, shall be credited against the reasonable cost of completing performance of the subcontract. If completed by the Obligee and the reasonable cost exceeds the balance of the subcontract price, the Surety shall pay to the Obligee such excess, but in no event shall the aggregate liability of the Surety exceed the amount of this bond. If the Surety arranges completion or remedies the default, that portion of the balance of the subcontract price as may be required to complete the subcontract or remedy the default and to reimburse the Surety for sums would have been payable to Principal had there been no default under the subcontract. The term "balance of the subcontract price," as used in this paragraph, shall mean the total amount payable by Obligee to Principal under the subcontract and amendments thereto, less the amounts heretofore properly paid by Obligee under the subcontract.

(emphasis added).

Jennifer Builders began work on the Project in March 1997. By May 1997, Siegfried had hired other subcontractors on a time and materials basis to perform some of Jennifer Builders' subcontract work. Siegfried, however, failed to notify Gulf that it had hired other subcontractors to perform Jennifer Builders' work. In fact, not until July 28, 1997 did Siegfried contact Gulf regarding Jennifer Builders' performance on the Project.

On July 28, 1997, Siegfried sent a letter to Gulf. In this July 28th letter, however, Siegfried did not declare Jennifer Builders to be in default, did not state that Jennifer Builders was to be considered in default of its subcontract and did not make a claim against Gulf as surety. In this letter, Siegfried also did not request that Gulf take any action pursuant to the performance bond or otherwise.[1] Instead, Siegfried stated only that it would "almost certainly" submit a claim to Gulf and that it had supplemented and performed some of Jennifer Builders' work.

Siegfried did not terminate Jennifer Builders. Siegfried threatened to terminate Jennifer Builders in a series of letters dated July 14, 1997, July 15, 1997, July 22, 1997 and July 26, 1997, but Siegfried wrote the threatening letters to urge Jennifer Builders to accelerate and finish its work. Siegfried also sent similar letters to other subcontractors on the Project likewise threatening to terminate those subcontractors, and Siegfried did not terminate those subcontractors either. Siegfried did not copy Gulf on the July 14th, 15th, 22nd or 26th letters sent to Jennifer Builders but only sent those letters as an attachment to the July 28th letter sent to Gulf. On August 5, 1997, the Surety acknowledged receipt of Siegfried's July 28th letter. In this letter, the Surety notified Siegfried that it had retained COP, Inc. to verify the information contained in the July 28th letter by contacting the Principal. As part of its investigation, COP, Inc. also contacted Siegfried, but despite this opportunity to request that the Surety perform pursuant to the performance bond, Siegfried did not request that Gulf complete Jennifer Builders' work. Jennifer Builders continued to work on the Project through August 1997 and

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[1]Had Siegfried declared Jennifer Builders to be in default, Gulf would have had the option of completing Jennifer Builders' work, arranging for Siegfried to complete Jennifer Builders' work or funding Jennifer Builders to complete its work.

into September 1997. The Project was substantially completed on September 19, 1997.

B. The Proceedings Below

In January 1998, Siegfried submitted a claim on the Performance Bond to Gulf. Gulf denied Siegfried's claim. Siegfried then filed suit in Virginia state court against Jennifer Builders for breach of contract and against Gulf on the Performance Bond. Jennifer Builders and Gulf removed the case to the United States District Court for the Eastern District of Virginia sitting in diversity. A non-jury trial was held by Judge Albert V. Bryan, Jr. of the United States District Court. At the conclusion of Siegfried's case, the court denied Jennifer Builders' Motion for Judgment as a Matter of Law but granted Gulf's Motion for Judgment as a Matter of Law. The court held that Siegfried failed to declare Jennifer Builders in default and failed to provide reasonable notice to Gulf as required by the performance bond. Before the trial could continue, Siegfried and Jennifer Builders stipulated to the amount of damages and the court entered judgment for Siegfried against Jennifer Builders.

Siegfried timely appealed the court's ruling granting Gulf's Motion for Judgment as a Matter of Law to the Fourth Circuit Court of Appeals on December 12, 1998. Oral argument was held on October 28, 1999. On February 2, 2000, the Fourth Circuit Court of Appeals reversed the lower court's ruling and remanded the case for a retrial in the United States District Court for the Eastern District of Virginia. In reversing the lower court's ruling, the Fourth Circuit held that obligees are not required to terminate a principal to invoke a surety's obligations under a performance bond unless such a provision is explicitly set forth in the performance bond, and in this case, such a provision did not exist. In other words, the Fourth Circuit Court of Appeals held that termination need not precede a declaration of default. While the Fourth Circuit Court of

Appeals found that the evidence produced at trial indicated that Gulf received the reasonable notice required under the Performance Bond, it is the position of the petitioner that the obligee must have terminated the principal before invoking, by notice, the surety's bond obligations.

REASONS FOR GRANTING THE WRIT

I. THE PETITION SHOULD BE GRANTED BECAUSE THE OPINION BELOW CONFLICTS WITH THE RULING OF THE FIFTH CIRCUIT COURT OF APPEALS

Gulf's petition for writ of certiorari should be granted because the opinion of the Fourth Circuit Court of Appeals conflicts with the Fifth Circuit Court of Appeals' ruling on the issue of whether an obligee must terminate a principal subcontractor under a performance bond to invoke the surety's obligations under the bond.

Before Gulf had any obligation under the Performance Bond, Jennifer Builders had to be in default "and be declared by Obligee to be in default." Gulf argued and the District Court held that a declaration of default to invoke Gulf's obligation under the Performance Bond required termination of the subcontract. The Fourth Circuit, however, disagreed and reversed the lower court's decision holding that to declare a principal in default and invoke the surety's obligations under a performance bond does not require termination of the principal.

In contrast, the Fifth Circuit in L & A Contracting Company v. Southern Concrete Services, 17 F.3d 106 (5th Cir. 1994), considered the identical bond provisions and virtually identical facts found in this case and held that a declaration of default to invoke the surety's obligations under a performance bond requires termination of the principal. In L & A Contracting, the Fifth Circuit found that Southern Concrete Services ("Southern"), the

subcontractor/principal, had breached the subcontract. The Fifth Circuit also found that L & A Contracting Company ("L & A"), the owner/obligee, repeatedly complained to Southern about Southern's performance and had sent numerous letters to Southern and its surety stating that Southern had breached the contract, giving Southern five days to cure the deficiencies in its performance, and even requesting that the bonding company take the necessary steps to fulfill the contract. L & A, however, never terminated Southern, and Southern completed its obligations under the subcontract. The surety took no action pursuant to the performance bond.

The Fifth Circuit held that the surety was not obligated under the performance bond because L & A failed to declare Southern in default. L & A, like Siegfried in this case, argued that "declared in default" meant only that it had to communicate that Southern had breached its duties under the subcontract. The Fifth Circuit rejected L & A's argument for three (3) reasons. First, L & A's argument failed to recognize the distinction between "breach" and "default." Not every breach rises to the level of a default sufficiently serious to justify termination. Second, a clear event must trigger the surety's right and obligation to step into the job and perform under the bond. Third, a surety is entitled to a clear notice that it has to perform.

The Fifth Circuit summarized the requirements of a declaration of default.

> We conclude, therefore, that [the surety's] is the only reasonable view. A declaration of default sufficient to invoke the surety's obligations under the bond must be made in clear, direct and unequivocal language. The declaration must inform the surety that the principal has committed a material breach or series of material breaches of the subcontract, that the obligee regards the subcontract as

> terminated, and that the surety must immediately commence performing under the terms of its bond.

Id. at 111. In other words, a surety is entitled to know what is being demanded from it and when it is expected to perform, and a declaration of default sufficient to invoke a surety's obligation under a performance bond requires termination of the principal. The Fifth Circuit held that Southern's breach of the subcontract and L & A's letters to Southern and the surety failed as a matter of law to establish a declaration of default.

The Fourth Circuit, in its opinion, specifically noted that other courts, including the Fifth Circuit, had reached a different decision on the question presented herein as to whether termination is required to establish a declaration of default. Despite the Fifth Circuit's ruling in L & A Contracting, however, the Fourth Circuit equated breach and default and held that Siegfried did not have to terminate Jennifer Builders to declare Jennifer Builders in default and invoke Gulf's obligation under the Performance Bond. The Fourth Circuit further diverged from the opinion of the Fifth Circuit in L & A Contracting when it held that a surety is not vulnerable to a suit for tortious interference of contractual relations in the event that a surety exercised its options under the bond absent termination of its principal. As held by the Fifth Circuit in L & A Contracting, the reason that the bond requires a declaration of default is because of the legal consequences that attend a surety's performance under the bond before the obligee considers the subcontract terminated. If a surety interferes in the affairs of its principal before a declaration of default, the surety faces possible tort liability. See L & A Contracting, 17 F.3d at 111 n.15(citing Gerstner Elec., Inc. v. American Ins. Co., 520 F.2d 790 (8th Cir. 1975) and Restatement (Second) of Torts §§ 766, 766A (1979)). Prior to default, a surety does not have a unilateral right to intervene in a contract dispute between an owner and

a principal unless the indemnity agreement between the surety and principal provides otherwise. Id.

Other courts have followed the Fifth Circuit. In Balfour Beatty Construction, Inc. v. Colonial Ornamental Iron Works, 986 F. Supp. 82 (D.Conn. 1997), the District Court for the District of Connecticut considered a bond provision identical to the one in L & A Contracting and the instant case and granted summary judgment to the surety because the obligee's numerous letters complaining about the subcontractor did not constitute a declaration of default. The court found that the fact that the obligee did not terminate the principal and allowed the principal to complete the project denied the surety the opportunity to exercise any of its options under the performance bond and the letters sent by the general contractor failed to provide sufficient notice of default. The court held:

> Performance bond requirements for notice of default and demand that the surety step in and perform under the bond must be met before an obligee can recover damages under the performance bond. Further, the language of the performance bond required: 1) that the principal be in default; and 2) that the obligee declare the principal to be in default so as to allow the surety to step in and take over the principal's obligations under the contract. The plaintiff in the present case allowed Colonial to complete the project, thereby denying the defendant the opportunity to exercise any of its options under the performance bond.

Learned commentary in this area further recognizes that a declaration of default means a termination of the bond principal's rights under the bonded contract. For example, Klinger and Diwik, "The Contract Performance Bond" in

Gallagher, ed. The Law of Suretyship, (American Bar Association 1993), states at p. 7-5: "However, for purposes of reviewing the Surety's options under the performance bond, it is assumed herein that the obligee timely terminated the principal for good cause." Dreifuss, "Bond, Contractual and Statutory Provisions and General Agreement of Indemnity" in Clore, ed. Bond Default Manual, Second Edition (American Bar Association, 1995), at p. 8, states that "this book pertains to bond defaults which, stated differently, are terminations for default...."

Gulf's petition should be granted so that the Court may resolve a split between the circuit courts on the issue of whether termination of a principal must precede a declaration of default to invoke a surety's obligations under the bond.

II. THE PETITION SHOULD BE GRANTED BECAUSE OF THE IMPORTANCE OF RESOLUTION OF THIS ISSUE TO THE CONSTRUCTION INDUSTRY AND THE SURETY INDUSTRY

This issue is not unique to this Project. The Fourth Circuit explicitly recognized the importance of resolution of the issue presented in this petition for writ of certiorari noting that "equating termination with default could effect a major change in the construction industry." How this issue is decided will affect significantly the construction industry's and the surety industry's way of doing business. As the Fourth Circuit recognized, the actual termination of a subcontractor is disruptive to a construction project and general contractors try to avoid making the decision to terminate. A requirement of termination, however, is for the Surety's protection and benefit. After the subcontract is terminated, the Surety can begin performance under the Bond without risking claims by the original subcontractor that the Surety has tortiously interfered with the subcontract,

and the Surety has an opportunity to mitigate its damages by acting promptly to obtain a completion contractor at the best available price. Without a bright line rule, however, both the construction industry and the surety industry will be forced to continue operating in a state of uncertainty when such a situation arises.[2] Uncertainty in the construction industry gives rise to increased judicial disputes which in turn diverts monies from the construction industry, an integral contributor to the overall economy.

Gulf's petition should be granted so that the Court may resolve an important issue to the construction industry and the surety industry.

CONCLUSION

This case presents a question of great importance to the construction industry and the surety industry. If the opinion below is allowed to stand, the split between the Fifth Circuit Court of Appeals and the Fourth Circuit Court of Appeals will cause continuing uncertainty in both industries when such a situation arises regarding the performance of a principal under a performance bond. Such uncertainty is detrimental to the construction industry and the surety industry as well as the economy. By granting Gulf Insurance Company's petition for writ of certiorari, this Court can resolve the split between the circuits and correct the Fourth Circuit's decision.

Accordingly, Gulf Insurance Company respectfully requests that its petition for writ of certiorari be granted.

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[2]The bond in this case is based on the American Institute of Architects Form A311, and thus is not unique to this Project but rather is a bond used throughout the construction industry.

Respectfully submitted,

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UNPUBLISHED

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 98-2808

SIEGFRIED CONSTRUCTION, INCORPORATED,
Plaintiff-Appellant,

v.

GULF INSURANCE COMPANY,
Defendant-Appellee,

and

JENNIFER BUILDERS, INCORPORATED, t/a Jennifer Drywall, Incorporated,
Defendant.

ASSOCIATED BUILDERS AND CONTRACTORS OF VIRGINIA, INCORPORATED; THE SURETY ASSOCIATION OF AMERICA; AMERICAN INSURANCE ASSOCIATION,
Amici Curiae.

Appeal from the United States District Court
for the Eastern District of Virginia, at Alexandria.
Albert V. Bryan, Jr., Senior District Judge.
(CA-98-555-A)

Argued: October 28, 1999
Decided: February 2, 2000
Entered: February 2, 2000

Before WIDENER, WILKINS, and TRAXLER, Circuit Judges.

Reversed and remanded by unpublished per curiam opinion.

COUNSEL

ARGUED: Mark Peyser Friedlander, Jr., FRIEDLANDER & FRIEDLANDER, P.C., McLean, Virginia, for Appellant. Erica Swecker Beardsley, WATT, TIEDER, HOFFAR & FITZGERALD, L.L.P., McLean, Virginia, for Appellee. **ON BRIEF:** Maurice Baskin, David C. Mancini, Charles W. Durant, VENABLE, BAETJER & HOWARD, L.L.P., McLean, Virginia, for Amicus Curiae Associated Builders. Martha L. Perkins, AMERICAN INSURANCE ASSOCIATION, Washington, D.C.; Edward G. Gallagher, WICKWIRE GAVIN, P.C., Vienna, Virginia, for Amicus Curiae Surety Association.

Unpublished opinions are not binding precedent in this circuit. See Local Rule 36(c).

OPINION

PER CURIAM:

Siegfried Construction, Inc. ("Siegfried" or"SC") appeals from the district court's grant of judgment as a matter of law for Gulf Insurance Company ("Gulf"), the surety on behalf of Siegfried's subcontractor, Jennifer Builders, Inc. ("Jennifer"). The district court concluded that (1) Siegfried did not declare Jennifer to be in default, and (2) Siegfried did not provide Gulf with reasonable notice that Siegfried was arranging for the correction and completion of Jennifer's work. Based upon these findings, the district court determined as a matter of law that Siegfried had not met the requirements of the performance bond. We reverse and remand.

I.

Siegfried was the general contractor for the construction of a Sleep Inn Hotel in Rockville, Maryland. In this capacity, Siegfried hired numerous subcontractors to perform portions of the work. Siegfried engaged Jennifer to install dry wall and door frames, hang valances, and complete some trim and finishing work. The subcontract required Jennifer to obtain a performance bond, which Gulf issued shortly after Jennifer began work on the hotel.[1]

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[1] The performance bond, which incorporated the subcontract by reference, in pertinent part provides:

NOW, THEREFORE, THE CONDITION OF THIS OBLIGATION is such that, if Principal shall promptly and faithfully perform said subcontract, then this obligation shall be null and void; otherwise to remain in full force and effect.

> Whenever Principal shall be, and be declared by Obligee to be in default under the subcontract, the Obligee having performed Obligee's obligations thereunder:
>
> 1. Surety may promptly remedy the default subject to the provisions of paragraph 3 herein, or; 2. Obligee, after reasonable notice to Surety may, or Surety upon demand of Obligee may, arrange for the performance of Principals' obligation under the subcontract subject to the provisions of paragraph 3 herein;
> 3. The balance of the subcontract price, as defined below, shall be credited against the reasonable cost of completing performance of the subcontract. If completed by the Obligee, and the reasonable cost exceeds the balance of the subcontract price, the Surety shall pay to the Obligee such excess, but in no event shall the aggregate liability of the Surety exceed the amount of this bond. If the Surety arranges completion or remedies the default, that portion of the balance of the subcontract price as may be required to complete the subcontract or remedy the default and to reimburse

The Sleep Inn construction, however, did not proceed smoothly. The hotel was originally scheduled to be completed by August 9, 1997, but was not finished until September 19, 1997. In many cases the delays were caused by various subcontractors, including Jennifer. During the course of the construction, Siegfried repeatedly complained to Jennifer about the quality of work and the laborers provided. Specifically, Siegfried remonstrated that the metal door frames installed by Jennifer were crooked, dry wall was hung in the wrong sequences causing delays, piece workers hanging drywall had no designated foreman, only four to eight dry wall workers were on the job when more were needed to remain on schedule, dry wall was improperly fitted around electrical and plumbing boxes, and in many areas dry wall was improperly placed so that it bulged.

On July 14, 1997, Siegfried sent Jennifer a "Formal Notice of Termination for Failure to Perform." J.A. 183. The letter, in accordance with the subcontract[2], gave Jennifer

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> the Surety for its outlays shall be paid to the Surety at the times and in the manner as said sums would have been payable to Principal had there been no default under the subcontract. The term "balance of subcontract price," as used in this paragraph, shall mean the total amount payable by Obligee to Principal under the subcontract and amendments thereto, less the amounts heretofore properly paid by Obligee under the subcontract.

J.A. 17.

[2] Article X of the subcontract provided that:

> If, in the opinion of SC, Subcontractor shall at any time (1) refuse or fail to provide sufficient properly skilled workmen or materials of the proper quality, (2) fail in any respect to prosecute the work according to the current schedule, (3) cause, by any action or omission, the stoppage or delay of or interference with the work of SC or of any other builder or subcontractor, . . . or (8) by any other action, indicate

"three (3) days formal notification of [Siegfried's] intention to terminate your subcontract agreement for default, unless acceptable corrections are effected by July 17, 1997." J.A. 183. The letter then set forth a number of grievances regarding Jennifer's workers and demanded that Jennifer take corrective action. On July 15, Siegfried sent a corrected termination letter to Jennifer further detailing problems with Jennifer's work and demanding prompt correction. Jennifer responded by making some changes, but Siegfried soon found that the original problems reoccurred.

On July 22, Siegfried sent a "Second Notice of Termination for Failure to Perform." J.A. 188. The second notice informed Jennifer that "Siegfried Construction intends, at its discretion, to terminate your subcontract agreement or to supplement your work forces in order to complete your work and the project on time." J.A. 188. The letter stated that Jennifer had failed to remedy the problems outlined in previous letters and set forth a schedule for the completion of Jennifer's work.

On July 26, Siegfried sent a "Follow-up to Second Notice of Termination for Failure to Perform." J.A. 190. Siegfried averred that "progress has not been maintained on

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> an unwillingness or inability to perform, or continue performing, hereunder then, after serving three days' written notice, unless the condition(s) specified in such notice shall have been eliminated within such three days, SC may, at its option (i) without voiding the other provisions of this Subcontract and without notice to Subcontractor's sureties, if any, take such steps as are necessary in SC's reasonable discretion, to overcome the condition(s), in which case the Subcontractor shall be liable to SC for the full cost thereof, (ii) terminate the Subcontract for default, or (iii) seek specific performance of Subcontractor's obligations hereunder, it being agreed by Subcontractor that specific performance may be necessary to avoid irreparable harm to SC and/or Owner. . . .

J.A. 170.

certain key work activities and necessitates that [Siegfried] supplement your manpower with personnel capable of performing with acceptable quality of workmanship." J.A. 190. The supplementation was in accordance with Article X of the subcontract agreement. The letter contained a revised schedule for the completion of Jennifer's work and provided that Siegfried would notify Gulf of the problems unless Jennifer could show marked improvement.

Not satisfied with Jennifer's progress, Siegfried sent Gulf a "Notice of Claim" on July 28 in which Siegfried announced that it would "almost certainly submit a claim for reimbursement of costs associated with completing and correcting work performed by Jennifer." J.A. 197. By this communication, Siegfried also informed Gulf of the supplementation of Jennifer's workforce and Siegfried enclosed copies of the letters sent to Jennifer which threatened termination.

Gulf forwarded Siegfried's communication to COP, Inc. ("COP"), Gulf's investigator. On August 5, COP informed Siegfried that it had been retained "to investigate claims against[Jennifer's] bond." J.A. 198. COP acknowledged receipt of the letters Siegfried had sent to Jennifer and promised to contact Siegfried at the end of the investigation.

Shortly thereafter, Siegfried discussed the claim with COP in a telephone conversation. Siegfried presented evidence that it told COP that it "needed some help" either from Gulf or Jennifer to complete the work on the hotel. J.A. 107. Siegfried did not hear from COP or Gulf while construction proceeded, and there is some dispute concerning Jennifer's abandonment of the job. However, all parties agree that Siegfried never terminated Jennifer. In January 1998, Siegfried submitted a claim on Jennifer's bond which Gulf refused to pay. Siegfried then brought suit in Virginia state court against Jennifer for breach of contract and against Gulf on the bond. The defendants removed the case to federal court, where a non-jury trial was held. At the

conclusion of Siegfried's case, the court heard motions for judgment as a matter of law from Jennifer and Gulf. The court denied the former's motion, but granted the latter's. In ruling in Gulf's favor, the district court found that the July 28, 1997 letter to Gulf was not a proper declaration of default nor reasonable notice that Siegfried was arranging for the performance of Jennifer's contractual obligation. The case proceeded no further because Siegfried and Jennifer then stipulated to the amount of damages and the court entered judgment for Siegfried against Jennifer. Siegfried now appeals the court's grant of Gulf's motion for judgment as a matter of law.

II.

For a grant of judgment as a matter of law pursuant to Federal Rule of Civil Procedure 52(c), we review the district court's legal conclusions de novo, see Freeman v. Case Corp., 118 F.3d 1011, 1014 (4th Cir. 1997), cert. denied, 118 S. Ct. 739 (1998), and its findings of fact for clear error, see Carter v. Ball, 33 F.3d 450, 457 (4th Cir. 1994). Judgment as a matter of law is appropriate when, without weighing the credibility of witnesses, there can be but one reasonable conclusion as to the correct judgment. See Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 250 (1986). If, however, evidence viewed in a light most favorable to the nonmovant indicates that more than one conclusion is plausible, judgment as a matter of law is improper. Id. at 250-51. Because the appeal from the district court is before us in diversity, see 28 U.S.C.A. § 1332 (West 1993 & Supp. 1998), we are bound by the substantive law of Virginia, see 28 U.S.C.A. § 1652 (West 1994); Erie R.R. Co. v. Tompkins, 304 U.S. 64, 78 (1938), and the parties agree that Virginia law is controlling.

A.

Siegfried first challenges the district court's determination that Siegfried never declared Jennifer to be in default. A performance bond is simply a contract and thus we turn to Virginia's principles of contract interpretation to guide the resolution of this issue. The court's task is to enforce contracts as written, not to unilaterally alter the parties' obligations. See D.C. McClain, Inc. v. Arlington County, 452 S.E.2d 659, 662 (Va. 1995). In Virginia, surety bonds are liberally construed, see Fidelity & Deposit Co. v. A.J. Bailey, 133 S.E. 797, 797 (Va. 1926), and "[s]ureties for hire" are required to "abide by their contracts and pay everything which by fair intendment can be charged against them." C.S. Luck & Sons, Inc. v. Boatwright, 162 S.E. 53, 54 (Va. 1932).

Under the performance bond, Gulf is liable for Jennifer's breach of contract if two conditions occur: (1) Jennifer is in default, and (2) Siegfried declares Jennifer to be in default. Siegfried argues that it declared Jennifer in default by virtue of the four notices of termination and the July 28, 1997 notice of claim sent to Gulf.

1.

To determine whether there was a proper declaration of default, we must first define a "default," a term that neither the bond nor the subcontract specifically explicate. In general, a default is defined as "the omission or failure to perform a legal or contractual duty." Black's Law Dictionary 417 (6th ed. 1990). According to the Virginia Supreme Court, a "building contractor defaults in the performance of his contract if he furnishes defective materials or workmanship." Clevert v. Jeff W. Soden, Inc., 400 S.E.2d 181, 183 (Va. 1991). Stated another way, "a builder's breach in the performance of his contract, i.e., a defective performance, also would be a `default' in that contract." Id.

The subcontract before us, though not specifically defining default, describes a "failure to perform" as follows: failure to provide skilled workers and quality materials; failure to complete work on time, causing delays for Siegfried or other subcontractors; or any other action indicating an inability or unwillingness to perform. "When contract terms are clear and unambiguous, the words used by the parties must be given their plain and ordinary meanings." Gordonsville Energy v. Virginia Elec. & Power Co., 512 S.E.2d 811, 817 (Va. 1999).

Siegfried's uncontradicted evidence indicates that the workers Jennifer provided were too few and without adequate supervision, that workmanship was substandard, and that Jennifer's deficiencies were causing delays in construction. Viewing this series of failings in a light most favorable to Siegfried, Jennifer's failure to perform was defective, material, and "defeat[ed] an essential purpose of the contract." Horton v. Horton, 487 S.E.2d 200, 204 (Va. 1997); see also RW Power Partners v. Virginia Elec. & Power Co., 899 F. Supp. 1490, 1496 (E.D. Va. 1995) (stating that under Virginia law a material breach deprives the party of an expected benefit and "goes to the root of the contract") (internal quotation marks omitted). As the provisions of the subcontract and the performance bond must be read together, see New Amsterdam Cas. Co. v. Moretrench Corp., 35 S.E.2d 74, 77 (Va. 1945), we conclude that the evidence presented during Siegfried's case in chief demonstrates that Jennifer was in default.

2.

Turning next to the second condition of the bond, the declaration of default, the district judge concluded as a matter of law that Siegfried never declared Jennifer to be in default. We disagree.

We are aware that the evidence in this case is not complete; and in passing on a challenge to a judgment as a matter of law, we must view the evidence in a light most favorable to Siegfried. In so doing, we find that Siegfried's evidence was sufficient to establish that it declared Jennifer in default. In communications to Jennifer and Gulf, Siegfried outlined the problems with Jennifer's laborers, their work, and the resulting delays. Siegfried repeatedly threatened Jennifer with formal termination for default if changes were not implemented[3]. These communications could reasonably be interpreted as pronouncements that Jennifer was not fulfilling its fundamental contractual obligations and that a claim for payment under the bond would be forthcoming. Thus, Siegfried presented sufficient evidence that it complied with the bond's condition that Jennifer be declared in default.

In support of the district court's ruling, Gulf avers that Siegfried's statement that it would "almost certainly submit a claim for reimbursement" was equivocal and cannot be interpreted as a declaration of default. J.A. 197. However, under the bond, Siegfried could collect from Gulf only if the reasonable cost of completion exceeded the balance of the subcontract. Thus, Siegfried could not have known the amount of its claim, if any, until it completed the work originally assigned to Jennifer. Under the terms of the bond, Siegfried could not have made a more definite statement regarding the specific amount of the likely claim.

Gulf further argues that Siegfried had to actually terminate Jennifer to declare default. Though other courts have required obligees to terminate a subcontractor to invoke a surety's obligations, see L & A Contracting Co. v. Southern Concrete Servs., Inc., 17 F.3d 106, 111 (5th Cir. 1994); Balfour Beatty Constr., Inc. v. Colonial Ornamental Iron Works, Inc., 986 F. Supp. 82, 85-86 (D. Conn. 1997),

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[3] Though Siegfried did not initially copy Gulf on the four notices of termination sent to Jennifer, Gulf did receive these letters when Siegfried submitted the July 28, 1997 notice of claim to Gulf.

Virginia law does not counsel this result. Had the parties intended that Siegfried actually terminate Jennifer before making a claim on the bond, "such a provision would surely, in clear language, have been inserted in the bond." Phoenix Ins. Co. v. Lester Bros., Inc., 127 S.E.2d 432, 436 (Va. 1962). Were the court to read such a requirement into the bond, we would be drafting rather than enforcing the bond as written. See D.C. McClain, Inc., 452 S.E.2d at 662 (stating that courts must enforce contracts as written).

Moreover, equating termination with default could effect a major change in the construction industry in Virginia. When the general contractor notices deficiencies in a subcontractor's work, generally all parties benefit if the subcontractor remains on the job. This common practice keeps the subcontractor working and permits the correction of problems and mistakes. The actual termination of a subcontractor is disruptive to the entire construction process because it adds to delays and expenses as new subcontractors must be found and retained, often at higher rates because of the premium paid for availability.

Similarly, Gulf contends that its involvement in the construction of the Sleep Inn -- absent Jennifer's termination-- could have resulted in Jennifer bringing a suit for tortious interference with contractual relations[4] We find this to be an unlikely result. Considering that Siegfried arranged for the correction and completion of Jennifer's work, it is unclear how Gulf would have been faced with a suit for tortuous interference had it simply paid the claim. Likewise, Gulf's exercise of other options under the bond,

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[4] The elements of tortious interference with contractual relations are as follows: "`(1) the existence of a valid contractual relationship or business expectancy; (2) knowledge of the relationship or expectancy on the part of the interferor; (3) intentional interference inducing or causing a breach or termination of the relationship or expectancy; and (4) resultant damage to the party whose relationship or expectancy has been disrupted.'" Century-21 v. Elder, 391 S.E.2d 296, 298-99 (Va. 1990) (quoting Chaves v. Johnson, 335 S.E.2d 97, 102 (Va. 1985)).

such as arranging for the completion of Jennifer's work, could not have been the cause of a breach of the subcontract or Jennifer's termination. Jennifer's failure to perform prior to the declaration of default would be considered the cause of a breach or termination. Even assuming Gulf's fear has some merit, the danger arises from the wording of Gulf's own bond. If Gulf believes termination is necessary to avoid a tortious interference suit, the better course would be to add this requirement to its performance bond. As the bond currently reads, the obligee is simply required to declare default, not terminate the principal.

Furthermore, Gulf's assertion that termination was a necessary component of a declaration of default is inconsistent with Gulf's conduct. In response to Siegfried's notice of claim, Gulf's investigator promised to contact Siegfried after it reviewed the claim. If termination of Jennifer was the determining factor triggering Gulf's responsibilities under the bond, then Siegfried could reasonably have expected Gulf to say so immediately. Instead, Gulf's hiring of COP to investigate the matter and COP's initial response could easily have convinced Siegfried that payment or assistance would be forthcoming. In fact, Siegfried told COP that Siegfried needed help from Gulf or Jennifer to complete the work. In the face of this pronouncement, COP, Gulf's representative, voiced no impediment to Gulf's involvement. In sum, we conclude that Siegfried presented adequate evidence to find that it declared Jennifer in default. In so holding, we reject Gulf's argument that termination must precede a declaration of default.

B.

Siegfried next challenges the district court's conclusion that Gulf was denied its options under the bond because Siegfried neglected to provide reasonable notice that it was arranging for the correction and completion of Jennifer's work. Once Siegfried declared Jennifer in default,

there were three options under the performance bond: (1) Gulf could remedy the default, (2) Gulf, upon Siegfried's demand, could arrange for the performance of Jennifer's obligation, or (3) Siegfried, after reasonable notice, could arrange for the performance of Jennifer's obligation. Though not defined in the bond, reasonable notice is generally described as notice conveying the requisite information and permitting time for response. Cf. Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306, 314 (1950) (defining reasonable notice in the context of due process). Siegfried contends that its July 28, 1997 letter to Gulf and accompanying documents constituted reasonable notice that it was arranging for the performance of Jennifer's contractual duties. The first paragraph of the letter informed Gulf that Siegfried planned to submit a claim for payment under the bond. The second paragraph informed Gulf that Jennifer's "failure to perform has necessitated that the Obligee supplement the Principal's work resources to correct unacceptable work and to assist in completing the Principal's work so as to mitigate delays." J.A. 197. On August 5, 1997, Siegfried received a letter from COP, Gulf's investigator, acknowledging receipt of the notice of claim, and promising to investigate all claims against Jennifer's bond. Apparently, Siegfried then telephoned COP and explained that it needed help to complete Jennifer's work on the Sleep Inn. Siegfried had no further communications with COP, and Gulf did not object to Siegfried arranging for the completion and correction of Jennifer's work.

We disagree with the district court that Siegfried's communications cannot be interpreted as providing Gulf with reasonable notice or giving Gulf an opportunity to hire a replacement for Jennifer. Virginia courts have not been overly strict in interpreting the notice requirements of construction bonds. See Southwood Builders, Inc. v. Peerless Ins. Co., 366 S.E.2d 104, 106-07 (Va. 1988) (stating that the principles of strict construction do not apply in favor of sureties for hire); see also American Surety Co. of New York

v. Zoby, 130 S.E.2d 587 (Va. 1963). And the evidence presented -- viewed in a light most favorable to Siegfried -- indicates that Siegfried's July 28 letter conveyed the requisite information under the bond. Siegfried explained to Gulf that as a result of Jennifer's substandard workmanship and insufficient number of workers, Siegfried was augmenting Jennifer's workforce and thus arranging for the performance of Jennifer's contractual duties. Moreover, Siegfried presented evidence that during the telephone conversation with Gulf's investigator it asked for help in completing Jennifer's work. In light of this request for assistance and considering that the project was not completed until the middle of September, Gulf had time to respond and exercise its options under the bond.

Gulf attempts to buttress the district court's holding by pointing out that Siegfried had been supplementing Jennifer's workforce long before the July 28 letter. While this fact is relevant to the amount of damages claimed against Gulf, it has no bearing on whether notice was given. In sum, the evidence produced at trial, which we construe in a light most favorable to Siegfried, indicates that Gulf received reasonable notice that Siegfried was arranging for the performance of Jennifer's obligation.

III.

For the foregoing reasons, we conclude that the district court erred in awarding Gulf judgment as a matter of law. The judgment of the district court is reversed and this matter is remanded for further proceedings consistent with this opinion.

REVERSED AND REMANDED

IN THE UNITED STATES DISTRICT COURT FOR THE
EASTERN DISTRICT OF VIRGINIA
ALEXANDRIA DIVISION

SIEGFRIED CONSTRUCTION, INC.,	)
Plaintiff,	)
v.	)
GULF INSURANCE COMPANY	)
and	)
JENNIFER BUILDERS, INC.	)
t/a Jennifer Drywall, Inc.	)
Defendants.	)

CIVIL ACTION NO. 98-555-A

Entered November 18, 1998

ORDER

For the reasons stated from the bench after the plaintiff had finished presentation of its case, which the court adopts as it findings of fact and conclusions of law, it is hereby, pursuant to F.R.Civ.P. 52(c),

ORDERED that judgment as a matter of law is entered in favor of the defendant, Gulf Insurance Company against the plaintiff, Siegfried Construction Company, Inc., and this action is dismissed as to Gulf Insurance Company.

\s\
Albert V. Bryan, Jr.
United States District Judge

Alexandria, Virginia
November 18th, 1998

THE COURT: Well, insofar as Jennifer's motion is concerned, it seems to me the obligation to promptly and faithfully perform the obligations imposed on it by the subcontract carries an implicit, if not direct, obligation to perform the work in a workmanlike manner. And I think there is ample evidence that the work was done defectively.

I don't - - I reject the argument that expert testimony is a necessary prerequisite to any recovery for defective workmanship of the type that was described here. The evidence concerning the doors, the covering up of the openings, the tolerance at the bottom of the doors and the other work that was improperly done in my view does not require expert testimony to establish the standards prevalent in the industry or otherwise.

I do think there are some claims that do not survive. I think the $23,910 general conditions arising from the delay cannot survive. I am not satisfied at this stage - - And in a nonjury case, at this stage I don't have to give the plaintiff the benefit of every favorable inference, but I can decide the case when a party has been fully heard on it. But I don't think there is any delay damage that can be attributable to the defendant. There were all kinds of delays, some of which may be attributable to the defendant, but I am not persuaded that they have been shown with any specificity.

I don't think the pocket door claim can be allowed. Nor the additional supervisor. And there is some $1,700 item that the plaintiff conceded was not.

So, the motion by Jennifer for judgment as a matter of law will be denied except to the extent that I will deny the recovery for the $23,910 general conditions, the $25,000 for the pocket doors, the $14,383 for the additional supervisor and that other $1,700 claim that I can't remember what it was about.

Insofar as Gulf is concerned, its motion will be granted. The bond is clear, it seems to me, that the principal must be in default and declared to be in default. They may

have been - - Jennifer's conduct may have entitled the plaintiff to declare it in default, but it never did. And it do so for the very reasons Mr. Sigfried testified to, he didn't want to declare it in default or terminate it if he can avoid it. That costs everybody money, not only the defaulting contractor, but the plaintiff. It is delay, he has to go get a new subcontractor. It is probably going to cost more because the new subcontractor knows that he is in a jam. And so, he was trying not to default Jennifer. And while he may have been entitled to, he didn't.

And so, I find that the letter of July 28 is not a declaration that Jennifer is in default. Nor is it reasonable notice to the bonding company.

And at some point the bonding company has to be given the opportunity to come in and do this work itself. The first option it is given under the bond is to do the work itself; or, upon reasonable notice, the obligee can make arrangements to do it itself. Actually some arrangements had already been made before this July 28 letter ever went out.

And I don't think the response as exhibited by Defendant's Exhibit 80 constitute an acknowledgment that the July 28 letter is the reasonable notice.

I, therefore, find that the motion is to be granted insofar as Gulf Insurance Company is concerned, judgment entered in their favor, and the action will be dismissed as to them.

The case will continue as to Jennifer for a claim for those damages sought, less the ones I have said cannot be recovered.

Is there any possibility of some resolution of it short of continuing -

MR. ETELSON: May I have one moment, Your Honor?

THE COURT: Well, I don't mean that you have to tell me - -

MR. ETELSON: No. If I may have one second, I may be able to resolve this very quickly.

THE COURT: All right.

MR. ETELSON: Your Honor, the remaining defendant in this case is Jennifer Builders. I have spoken to the president of Jennifer Builders. Your Honor has knocked out a lot of the claims that we felt were inappropriate. In talking to the president, the difference between the maybe additional $10,000, even if we got on, and without prejudice to us, acknowledged that there were some problems with this, isn't worth going through an entire another day of trial.

So, therefore, given Your Honor's ruling, if we subtract out what Your Honor said, on the difference between the 106 and the remaining amount, we will allow a judgment ot be entered against Jennifer Builders and move on from there to save another day in court.

THE COURT: Well, I am not sure of the addition and subtraction in my head. Talk to Mr. Friedlander, see if that is a satisfactory resolution of the matter.

If he wants to go forward tomorrow to get more than the figures you have suggested - -

MR. ETELSON: I have given him the full amount of his case, Your Honor. What I am saying is, if we take the full amount of his claim, subtract out what Your Honor has dismissed in terms of the damages, we'll allow him to have that judgment now in order to save another day in trial. There is nothing else he can go for. He has completed his case in chief.

THE COURT: Well, I can't agree with you completely because I am not sure what his total claim is. There is 100- -

MR. FRIEDLANDER: Your Honor, I can address that if Your Honor will just give me a moment to do some arithmetic. We may accept his offer.

THE COURT: All right. Okay. I just want to make sure you are talking about the same figure. I don't

want to leave here and then say, you are talking abut one figure and Mr. Friedlander is talking about another. So - -

MR. ETELSON: The only reservation, Your Honor, is I guess attorney's fees haven't been addressed. Nothing had been entered into evidence on that.

MR. FRIEDLANDER: My understanding, on the issue of attorney's fees, is that first you win and then you are allowed to submit to Your Honor a claim for attorney's fees.

THE COURT: Yes. And I will take that up, give you 30 days to file your request for attorney's fees if that is not resolved too.

But why don't the two of you get together before you leave here tonight, see if you can't get together on a figure, including attorney's fees. And then if we need to go forward in the morning, we can.

If not, let me know in the morning and I will be delighted to hear from you. But if not we can hear from the defendant's case.

MR. ETELSON: How long do we have tonight, Your Honor, so that we don't have to come back tomorrow morning?

THE COURT: You have as long as you want. You don't have to come back tomorrow if you call me in the morning, and I will be here at 8 o'clock, and you tell me you all have resolved it, then you don't have to come back in the morning.

MR. ETELSON: Thank you.

THE COURT: But how long you take tonight doesn't make any difference to me. I don't require that you notify me tonight. I will put it that way.

MR. ETELSON: Thank you, Your Honor.

MR. FRIEDLANDER: Your Honor, just to be clear on one - - If we proceed with this arithmetic and resolve it, we do not waive any rights of appeal as to the bonding company.

THE COURT: Okay.

MR. FRIEDLANDER: And as long as whatever - -

THE COURT: Well, they have got a judgment in their favor now. I am not asking them to settle anything. The settlement I am suggesting you pursue is with Mr. Etelson.

MR. FRIEDLANDER: No, I understood, Your Honor. I just wanted to make sure I was very clear on the record.

THE COURT: If you can get some money out of the bonding company, fine, but they have got their foot in the door now and is not as easy to talk to, I expect, as it might have been earlier.

All right. If you - - Actually, would you let me know one way or another in the morning?

MR. ETELSON: Yes, Your Honor.

THE COURT: So I will know whether I am coming back into court at 10 o'clock or not coming back.

MR. ETELSON: Yes, Your Honor.

THE COURT: Thank you. Court will stand adjourned until tomorrow morning at 10 o'clock.

NOTE: The case was concluded at the is point, with the remaining issues having been settled in the course of the evening.

HEARING CONCLUDED

I certify that the foregoing is a true and accurate transcription of my stenographic notes.

\s_____
Norman B. Linnell, CP, CM, CE

MIDWEST INDEMNITY

SUBCONTRACTOR PERFORMANCE BOND
BOND NO. AE5917442

KNOW ALL MEN BY THESE PRESENTS, that JENNIFER BUILDERS, INC. t/a JENNIFER DRYWALL INC. 9021 SHADY GROVE COURT, GAITHERSBURG, MD, 20677 XXXXX Principal, hereinafter called Principal, and Gulf Insurance Company, 5550 West Touchy Avenue, Suite 400, Skokie, IL 60077, as Surety, hereinafter called Surety, are held and firmly bound unto SIEGFRIED CONSTRUCTION, INC. 8456 TYCO ROAD, VIENNA, VA 22182, as Obligee, herinafter called Obligee, in the amount of ONE HUNDRED SIXTY-FIVE THOUSAND and 00/100 DOLLARS ($165,000.00) for the payment whereof Principal and Surety bind themselves, their heirs, executors, administrators, successors, and assigns, jointly and severally, firmly by these presents.

WHEREAS, Principal has by written agreement dated OCTOBER 15th 1996 entered into a subcontract with Obligee for DRYWALL - WEST MONTGOMERY HOTEL HOLDINGS PROJECT - SLEEP INN, ROCKVILLE, MD in accordance with drawings and specifications prepared by _____ which subcontract is by reference made a part hereof, and is hereinafter referred to as the subcontract.

NOW, THEREFORE, THE CONDITION OF THIS OBLIGATION is such that, if Principal shall promptly and faithfully perform said subcontract, then this obligation shall be null and void; otherwise to remain in full force and effect.

Whenever principal shall be, and be declared by Obligee to be in default under the subcontract, the Obligee having performed Obligee's obligations thereunder;

Surety may promptly remedy the default subject to the provisions of paragraph 3 herein, or;

Obligee, after reasonable notice to Surety or Surety upon demand of Obligee may, arrange for the performance of Principal's obligation under the subcontract subject to the provisions of paragraph 3 herein;

The balance of the subcontract price, as defined below, shall be credited against the reasonable cost of completing performance of the subcontract. If completed by the Obligee, and the reasonable cost exceeds the balance of the subcontract price, the Surety shall pay the Obligee such excess, but in no event shall the aggregate liability of the Surety exceed the amount of this bond. If the Surety arranges completion or remedies the default, that portion of the balance of the subcontract price as may be required to complete the subcontract or remedy the default and to reimburse the Surety for its outlays shall be paid to the Surety at the times and in the manner as said sums would have been payable to Principal had there been no default under the subcontract. The term "balance of the subcontract price," as used in this paragraph, shall mean the total amount payable by Obligee to Principal under the subcontract and amendments thereto, less the amounts heretofore properly paid by Obligee under the subcontract.

Any suit under this bond must be instituted before the expiration of one year for the date on which final payment under the subcontract falls due.

No right of action shall accrue on this bond to or for the use of any person or corporation other than the Obligee

named herein or their heirs, executors, administrators or successors of the Obligee.

Signed and sealed this 1st day of April A.D., 1997.

In the presence of:

Gulf Insurance Company
Surety

/s/_____
LEONARD E. CALLAHAN
Attorney-in-Fact

JENNIFER BUILDERS, INC. t/a
JENNIFER DRYWALL, INC.
Principal

By /s/_____

RELEVANT SECTIONS OF PERFORMANCE BOND

NOW, THEREFORE, THE CONDITION OF THE OBLIGATION is such that, if Principal shall promptly and faithfully perform said subcontract, then this obligation shall be null and void; otherwise to remain in full force and effect.

Whenever Principal shall be, and be declared by Obligee to be in default under the subcontract, the Obligee having performed Obligee's obligations thereunder;

1. Surety may promptly remedy the default subject to the provisions of paragraph 3 herein, or;

2. Obligee, after reasonable notice to Surety may, or Suerty upon demand of Obligee may, arrange for the performance of Principals' obligation under the subcontract subject to the provisions of paragraph three herein;

3. The balance of the subcontract price, as defined below, shall be credited against the reasonable cost of completing the performance of the subcontract. If completed by the Obligee, and the reasonable cost exceeds the balance of the subcontract price, the Suerty shall pay the Obligee such excess, but in no even shall the aggregate liability of the surety exceed the amount of this bond. If the Suerty arranges completion or remedies the default, that portion of the balance of eth subcontract price as may be required to complete the subcontract or remedy the default and to reimburse the surety for its outlays shall b paid to the surety at the times and in the manner as said sums would have been payable to Principal had there been non default under the subcontract. The term :"balance of the subcontract price, : as used in this paragraph, shall mean the total amount payable by Obligee to Principal under the subcontract and amendments thereto, less the amounts heretofore properly paid by Obligee under the subcontract. (JA 17)

THIS PAGE (16A) CONTAINS RETYPING OF RELEVANT SECTION OF JOINT APPENDIX PAGE 17 MERELY AS CONVENIENCE TO THE COURT DUE TO SIZE OF TYPE AND POOR PAPER QUALITY